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COMMON FUND FOR COMMODITIES

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THE ROLE OF COMMODITIES IN LEAST DEVELOPED COUNTRIES

Note by the Common Fund for Commodities

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I. Introduction

1. Commodities remain the economic backbone of LDC economies, often comprising more than 90 per cent of merchandise exports. Governments rely on commodity export revenues for a large portion of their annual budgets and household income is often highly dependent on employment in the commodity sector. The future prospects of LDCs are also closely associated with developments in commodity markets for two reasons. First, as one of the major sectors in the economy, investment in this sector, particularly with regard to vertical diversification, will drive employment generation and economic growth. Second, given the relatively weak position of the financial sector in LDCs, private sector investment will be expected to be derived from profits. Moreover, as a major productive sector, the commodity sector itself can be expected to provide some of the surplus for investment across the economy, particularly with regard to diversification, to be supplemented by foreign direct investment (FDI).

2. In rural areas, the majority of the population is dependent, directly or indirectly, on the commodity sector for their livelihood. It is estimated that, overall, one billion people in developing countries derive a significant share of their income from export commodities; many of these people are to be found in LDCs. The viability of the commodity sector is therefore inextricably linked to future prospects for growth, employment generation and poverty reduction. If international development targets to halve world poverty by 2015 are to be attained then commodities must be placed centre-stage in the effort to promote economic growth and poverty reduction.

II. Commodities, Export Earnings and Indebtedness

3 Industrialized countries accounted for over half of world commodity exports in the mid-1990s. Nevertheless, the importance of commodities for national economies is very much greater in developing countries and in particular, in LDCs. Export dependence is a conventional measure of the degree of commodity dependence. Table 1 below has been compiled for those LDCs which exhibit export dependence greater than 50 per cent of total merchandise export earnings.

4. Table 1 highlights two important facts:

1. The importance of commodities for export earnings for LDCs has not declined significantly since 1980. Countries such as Chad, Guinea-Bissau, United Republic of United Republic of Tanzania and Cambodia have registered increased dependence on primary non-fuel commodities while the situation has barely changed for many others;

2. There is a close link between commodity dependence and indebtedness. Of the 48 LDCs, 29 are classified as Heavily Indebted Poor Countries (HIPCs), of which 27 have a commodity export dependence greater than 50 per cent (table 1). As debt sustainability is based on export ratios and as terms of trade decline, export revenues will also decline, resulting in an unsustainable burden of debt. More directly, however, the need to finance current account deficits through loans to off-set falling export revenues has resulted in higher levels of debt, unsustainable balance of payments and quite often, macroeconomic instability.

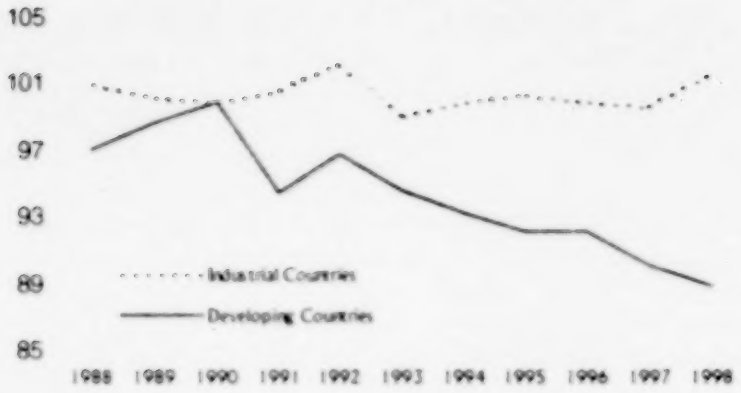
Table 1. COMMODITY EXPORT DEPENDENCE GREATER THAN 50 per cent FOR LEAST DEVELOPED COUNTRIES, 1997

Countries	Commodities as per cent of Merchandise Exports		Leading Commodities	GNP per capita		Poverty (PPP) per cent of Population living on less than $1 a day	
	1980	1997 unless otherwise stated		US$ 1997	Changes in per cent 1996-97	per cent	Year
Mauritania*	99.6	99.9	iron ore, fishery	440	2.1	31.4	1988
Chad*	85.4	99.9	cotton, meat	230	3.5		
Sao Tome and Principe		99.9	cocoa, copra, coffee	290	2.0		
Yemen, Rep*	53.0	99.4	fuels	270	-0.5		
Angola*	87.1	97.7	fuels	260	2.5		
Rwanda*	99.6	97.7	coffee, tea, tin ore	210	5.6	45.7	1983-85
Niger*	98.0	97.6	uranium, livestock	200	0.0	61.5	1992
Sudan*	99.2	97.2	cotton, animals, sesame seeds	290	4.2		
Guinea-Bissau*	91.8	95.8	nuts, fishery	230	4.4	88.2	1991
Burundi*	96.3	95.7	coffee, tea	140	1.5		
Somalia*		95.5	live animals, fishery, bananas				
Benin*	96.6	95.4 (1996)	cotton, fuels	380	2.7		
Gambia	91.2	92.8 (1996)	peanuts, fish, cotton lint, palm kernels	340	2.1		
Malawi*	93.6	92.7	tobacco, tea, sugar	210	2.5	4.3	1995
Myanmar*	92.8	89.6 (1991)	wood, pulses, rice				
Equatorial Guinea 1	95.4	89.5	Petroleum, timber, cocoa	1,060			
Ethiopia*	99.8	86.8	coffee	110	3.0	46.0	1981-82
Mali*	99.7	83.9	cotton, gold	260	3.5		
Mozambique*	61.8	83.3	fishery, nuts, cotton	140	10.5		
Guinea*	99.3	82.5 (1996)	bauxite, aluminium	550	1.9	26.3	1991
Togo*	89.4	80.5	phosphate rock, cotton, coffee	340	2.0		
United Republic of Tanzania*	65.9	78.2 (1996)	coffee, cotton, cashew nuts, minerals, tobacco, sisal	210	4.2		
Burkina Faso*	89.2	74.7	cotton	250	3.2		
Madagascar*	93.7	72.1	coffee, vanilla, cloves, shellfish, sugar	250	1.5	72.3	1993
Lao People's Democratic Republic	65.6	71.3 (1996)	wood, live animals, coffee	400	3.8		
Uganda*	99.3	70.7 (1996)	coffee, cotton	330	3.0	69.3	1989-90
Zambia*	84.0	68.5	copper, zinc	370	1.8	84.6	1993
Solomon Islands 1	81.2	66.5	Timber, fish, palm, copra	870			
Cambodia	35.8	65.8	wood, rubber, soybeans	300	-1.4		
Sierra Leone *	60.1	57.8 (1996)	diamonds, rutile, cocoa, coffee, fish	160	20.6		
Afghanistan 1	72.0	57.6	Dried fruit and nuts, wool and hides, cotton				
Central African Republic *	73.8	57.4	wood, live animals, cotton	320	3.8		

Source: World Bank 1998, UNCTAD 1998 and Common Fund for Commodities
*denotes eligibility for assistance under HIPC Debt Initiative 1 as per cent of total exports of goods and services

5. Figure 1 shows the decade-long decline in the terms of trade for developing countries as a group. Despite this marked decline, UNCTAD has noted that aid inflows over the past decade have not been sufficient to off-set foregone export revenues. In this regard, therefore, the net inflow of funds that is required to implement programmes which might stimulate growth and promote the reduction of poverty has not been forthcoming. The debate over the effectiveness of aid would do well to note this point as, in many cases, it may be that aid resources have simply compensated partly for lost export revenues rather than providing an additional source of finance.

Figure 1. Terms of Trade



6. The impact of indebtedness on growth and poverty reduction is most clearly demonstrated by the debt overhang. Where levels of debt are high, an expectation of increased future taxation (or deficit financing and associated higher levels of inflation) serves as a disincentive to foreign and domestic investment. Balance of payments sustainability, a major focus of IMF programmes, aims to build-up 4 to 6 months of reserves cover in recognition of increased probability of external shocks, of which exposure to declining commodity prices is just one. This reserve build-up results in larger quantities of resources set aside rather than made available for investment in poverty reduction programmes. Clearly, it is more difficult to build-up reserves during periods when commodity prices are low.

7. The adverse impact on growth, as regards current constraints on the balance of payments imposed by falling commodity prices and future uncertainty generated by the resultant debt overhang, cannot be overstated. In turn, this repressed level of growth and investment adversely affects prospects for diversification, resulting in lower rates of employment growth and higher levels of poverty.

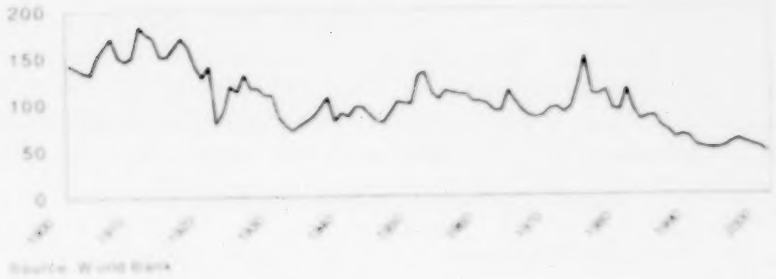
III. Trading Environment and Price Levels

8. Since 1980, global trade in commodities has more than doubled while world GDP has expanded by over 90 per cent in real terms.[1] The real value of the 21 major commodities exported by all developing countries increased 59 per cent in the period 1970-1971 to 1996-1997. Virtually all of this growth, however, can be assigned to increased volume as real prices declined for nearly all of these commodities, over this period.[2] Commodities, such as palm oil, have seen the production value more than triple despite a halving of price (e.g. production increased nearly eight-fold) while the production value of cotton and coffee has declined despite increased output.

9. This is part of a broader trend, which saw global commodity prices decline in real terms for most of the twentieth century. Figure 2 clearly shows the general downward trend in real non-oil commodity prices and the volatility around the mean of 100. Since the 1970s the trend has been almost continually downward.

[1] Source: IMF, World Economic Outlook, October 1999 and UNCTAD Handbook of Statistics, 2000.
[2] World Bank, Global Commodity Markets, April 2000 p10.

Figure 2. Real Non-Oil Commodity Prices, 1900-2000



Source: World Bank

10. The current status of commodity markets for many agricultural and mineral products can be best understood by considering them in their economic context. This market context can then serve to give a better understanding of the underlying trends and policies that influence world prices and contribute to continued commodity dependence in many LDCs.

11. In 1998, LDCs accounted for only 0.38 per cent of world trade, however an important part of this trade comprised commodities, (see Table 2) which supports the data on individual countries presented in Table 1.

Table 2. Leading LDCs Exports

Item	Value	Per cent of LDC exports	per cent of world trade
Textiles	3,951.7	19.68	15.78
Petroleum (& products)	3,919.6	19.52	1.89
Cotton	1,593.2	7.94	14.31
Coffee	1,125.8	5.61	6.94
Fish (incl shelled)	1,121.1	5.58	6.73
Precious stones	782.9	3.90	2.15
Copper	549.7	2.74	1.83
Tobacco	387.3	1.93	5.85
Timber	378.8	1.89	4.94
Ores, base metals	341	1.70	1.77
Vegetables	304.8	1.52	1.3
Iron ore	284.3	1.42	2.83
Fruit and nuts	256.8	1.28	0.9
Leather	212	1.06	1.5
Floor coverings	208.1	1.04	2.02
All commodities	**20,076.5**	**100**	**0.38**

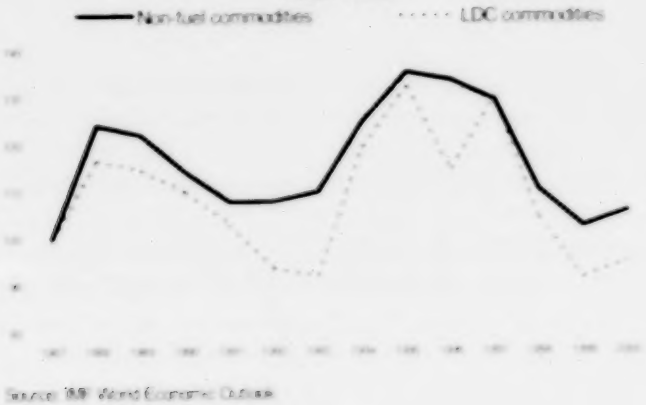
Source: UNCTAD LDC Report 2000

12. One of the major factors for the continued low commodity price levels is the ample levels of supply, indicated by the ratio of global stocks to annual consumption.[3] This level of over supply can, in part, be seen as a response to the economic reforms that have been implemented in many LDCs over the last two decades, particularly in the agricultural sector. This has removed the bias against exports (e.g. tariff protection on imports, taxation on exports and the overvaluation of the exchange rate) and has improved the incentives for commodity producers to boost exports. Subsidized exports and third market penetration by developed country producers have played a role in the case of several commodities. The strength of the United States dollar against most other currencies has also served to restrain commodity prices.

[3] In the case of cocoa (40 per cent in 2000), sugar (49 per cent in 1999), co- ton (37 per cent in 2000) and coffee (37.5 per cent in 1999) high stock to use ratios have led directly to the depressed prices of recent years.

13. Falling prices have led to significant deterioration in the terms of trade of LDCs . Of late, pressure of falling prices on current accounts has been exacerbated by rising oil prices. The initial adverse impact of rising oil import prices on oil-importing LDCs is compounded by the anticipated contractionary effects on the global economy which, notwithstanding the weaker correlation between world economic expansion and commodity demand, will drive down prices for other commodities (Figure 3).

Figure 3. Non-Fuel and LDC Commodity Prices, $
(1987 = 100)



Source: IMF, *World Economic Outlook*

14. A further price-related concern is that, although producer prices for commodities have been declining for an extended period, consumer prices have continued to rise: the price of raw coffee, for example, declined by 18 per cent on world markets between 1975 and 1993 but the consumer price increased by 240 per cent in the United States. In this regard the World Bank instigated an investigation and concluded that there was robust statistical evidence, both across commodities and countries, to support the hypothesis that there was a growing disparity between producer and consumer prices for commodities.[4]

15. This disparity is illustrated in Figure 4 which shows that, for 6 non-oil commodities (banana, beef, coffee, rice, sugar and wheat), there has indeed been an almost continuous increase in the price spread which has seen the disparity between producer and consumer prices almost double in the last two decades. Spreads declined in the early 1970s due to the commodity price boom and again at the end of this period due to falling consumer prices for

Figure 4. Commodity Producer Consumer Price Spread
(1990 = 100)

Source: Monsset 1997

[4] Monsset, 1997 (World Bank article)

coffee and sugar.

16. It has been estimated that this practice may have cost commodity exporting countries in excess of $100 billion per year due to constrained growth in demand. The existence of this asymmetry in price behaviour is attributed to the practices of international trading companies, many of which are large enough to exercise a degree of monopoly power in many commodity markets.

17. The global trading environment and, more specifically, the ability of LDCs to participate fully in the process of globalization is a major factor that contributes to prospects for growth. Trade offers the opportunity to increase export earnings (which finance increased levels of imports); instils competitive discipline on producers and allows the transfer of technology; and provides new markets and scope for economies of scale in production. However, despite efforts to liberalize, boost productivity and increase foreign investment flows, many LDCs have become increasingly marginalized in global trade. Important factors that have been identified to improve this scenario include the transfer of technologies, increased investment flows, technical assistance and the removal of structural rigidities that act as a drag on economic performance. The issue of market access, however, has been highlighted as a major obstacle to boosting export performance.

18. Apart from supply capacities, the ability to actually enter markets is fundamental. Even if market access was totally free and if supplies were available, success in entering markets would not be assured, particularly given the non-competitive market structures. Concessional arrangements, such as the Lome Convention (and more recently, the "everything but arms" initiative for LDCs) and the United States Africa Growth and Opportunity Act, which benefit many LDCs, have been introduced. However, there is growing evidence, which demonstrates that the real benefits of these arrangements are limited. In the twenty-five year existence of the Lome Convention, for example, the African, Caribbean and Pacific (ACP) countries have seen their share of European Union imports fall from 7 per cent to 3 per cent. Arguments advanced to explain the widespread failure of preferences include the use of other obstacles such as quota ceilings, limitations on coverage and a narrowing of preference margins through Most Favoured Nation (MFN) trade liberalization. It also shows that market access and enhancement of productive capacities must be linked. The new European Union-ACP treaty signed in 2000 - Cotonou Agreement, shifts the focus from trade toward a broader development agenda with poverty reduction at its core. Consequently, the STABEX mechanism, which compensated countries for declining export revenues derived from traditional commodities, has been discontinued in favour of a more holistic approach to development finance and support to the rural sector. While the assimilation of commodity issues into the broader process of rural sector development and growth may be welcome, the dilution of commodity-specific assistance increases the exposure of LDCs to commodity price volatility.[5]

19. The US Africa Growth and Opportunity Act, which was signed into law in May 2000, will widen access to the United States market, but has significant clauses (e.g. for textiles fabricated from local yarn, sugar, coffee) which may hinder the full exploitation of the opportunities afforded under the Act.

[5] Explanatory note on twin criteria of 1) a fall and 2) evidence of budgetary impact. Ex post verification and delays may mean that additional assistance does not operate as a counter-cyclical stabilization mechanism.

20. Despite the unilaterally applied limits on "enhanced" market access, more often domestic constraints have been cited, including a lack of physical, financial, human and institutional infrastructure, which has resulted in an inability to diversify or produce value-added goods. A failure to meet quality standards, particularly for new products and markets, also precludes the development of successful new export ventures. Consequently, LDC's have been unable to take advantage of the opportunities afforded by preferences.

21. The failure of some LDCs to overcome these constraints indicates that policy and institutional weaknesses must be addressed before new opportunities for trade can be fully exploited. Adopting a narrow definition of market access, therefore, risks oversimplifying the debate on trade and deflects attention from other related issues that are of equal significance.

IV. Price Fluctuations

22. Liberalization and the exposure of producers to the impact of global market forces has resulted in increased price volatility for producers. This, as well as the declining trend in prices, has become a major concern to commodity-dependent economies. One response has been to investigate the use of price risk management instruments, for example the use of put options which give the producer or trader the opportunity to sell at a contracted price. A study of the use of these instruments has been undertaken by the World Bank-led International Task Force (ITF), of which the Common Fund is a member - pilot projects to test their use are underway.[6]

23. The economic explanation for volatile and declining commodity prices is based on price and income elasticities. In the case of commodities, it has long been accepted that price and income elasticities of demand are low. This means that as incomes rise over time, commodity consumption does not increase at the same rate, resulting in stagnating levels of demand and consequently, falling prices. Similarly, low price elasticities mean that supply fluctuations are associated with large swings in prices and this volatility is compounded by the supply response of producers who may only be able to adjust production with a considerable lag (e.g. the short term supply response is near zero), resulting in the cyclical troughs and peaks often observed in prices for individual commodities. The result of this relationship between supply, demand and prices is that commodity export earnings have been both declining and have remained unstable for an extended period.

24. A recent study by the World Bank used historical perspective to consider the main contributory factors to the process of economic growth.[7] One of the reports main findings was that sustained periods of stable growth and income stability were more conducive to robust poverty reduction than periods which featured cyclical patterns of "boom and bust". Therefore, the lesson for LDCs and the international donor community is clear: commodity price volatility is a source of instability that undermines prospects for steady economic growth and need be addressed. Complementary to this task is the need to provide assistance consistent with a country's national development plan to improve productivity and quality. Common Fund financed projects address the issues of productivity, quality, standards, market development, processing and branching out of traditional production structures. Through this

[6] The first such project, financed by the Common Fund, was approved in April 2000 and will assess the feasibility of using such instruments in the cocoa sector in West Africa. Two more projects are in the pipeline, on coffee and on cotton in East Africa.

[7] World Bank, The Quality of Growth, 2000.

assistance, export markets will be secured and the prospects to embark on a stable growth path will be maximized.

25. Export dependence also exposes LDCs to shocks and increases the volatility of revenues. This is not exclusively restricted to exposure to price fluctuations in global markets but also applies to localized shocks such as adverse weather and disease blight. The resultant uncertainty has both micro and macroeconomic impacts. At the farmer level it may result in a sub-optimal allocation of resources, as minimizing risk displaces maximizing profits as the dominant household strategy. Macroeconomic impacts are often felt through a boom and bust scenario where fiscal windfalls resulting from commodity price increases are not efficiently invested (either by the public or private sector). Conversely, periods of low commodity prices lead to deteriorating terms of trade. This places pressure on the balance of payments (as outlined above), chokes off investment and retards growth.

V. Commodity Output and Productivity in LDCs

26. The decline in the terms of trade clearly highlights the need to boost output and/or improve productivity to lower the costs of production (and thereby increase profit margins). As outlined above, the aggregate response of developing countries has led to an over supply of many commodities in the global market place, resulting in further deterioration in commodity prices. This scenario is labelled "the fallacy of composition" as it disproves the belief that, as a group, LDCs, or indeed, developing countries generally, can boost export revenues by increasing production. The focus must therefore be placed, at least in the first instance, on improving productivity. The investible surplus may then be channelled into other productive sectors and for diversification. Table 3 identifies those LDCs that are successfully increasing either output or productivity in their respective commodity sectors.

Table 3. Output and Productivity in LDCs

Product	Countries with increasing output and increasing productivity	Countries with increasing output and decreasing or stagnant productivity	Countries with increasing productivity and decreasing or stagnant output	Countries with decreasing or stagnant productivity and decreasing or stagnant output
Cocoa	Dem. Rep. of Congo, Guinea, Madagascar, United Republic of Tanzania, Uganda, Vanuatu	Haiti, Solomon Islands	Sierra Leone	Equatorial Guinea, Liberia, Sao Tome and Principe, Samoa, Togo
Coffee	Ethiopia, Guinea, Malawi, Sierra Leone, Togo, Uganda, Zambia	Lao People's Democratic Republic, Myanmar, Yemen	Central African Republic	Angola, Benin, Burundi, Dem. Rep. of Congo, Equatorial Guinea, Haiti, Liberia, Madagascar, Mozambique, Rwanda, United Republic of Tanzania
Jute	Ethiopia, Madagascar, Mozambique	Mali	Bangladesh, Cambodia, Nepal	Angola, Myanmar, Cambodia
Seed cotton	Afghanistan, Angola, Bangladesh, Benin, Chad, Gambia, Guinea, Lao People's Democratic Republic, Malawi, Mozambique, Myanmar, Somalia, United Republic of Tanzania, Togo, Uganda	Burkina Faso, Mali	Central African Republic, Dem. Rep. of Congo, Sudan, Yemen	Burundi, Cambodia, Ethiopia, Guinea Bissau, Haiti, Madagascar, Niger
Sugar	Benin, Burkina Faso,	Bangladesh, Liberia,	Angola, Haiti	Afghanistan, Ethiopia,

Product	Countries with increasing output and increasing productivity	Countries with increasing output and decreasing or stagnant productivity	Countries with increasing productivity and decreasing or stagnant output	Countries with decreasing or stagnant productivity and decreasing or stagnant output
cattle	Burundi, Cambodia, Cape Verde, Chad, Dem. Rep. of Congo, Guinea, Lao People's Democratic Republic, Madagascar, Mali, Nepal, Sudan, United Republic of Tanzania, Uganda	Malawi, Myanmar, Niger, Zambia		Mozambique, Rwanda, Sierra Leone, Somalia
Tea	Bangladesh, Burundi, Ethiopia, Lao People's Democratic Republic, Nepal, Rwanda, Uganda	Malawi, Myanmar, United Republic of Tanzania		Dem. Rep. of Congo, Mozambique
Tobacco	Angola, Cambodia, Ethiopia, Malawi, United Republic of Tanzania, Uganda	Dem. Rep. of Congo, Lao People's Democratic Republic, Madagascar, Rwanda, Zambia	Bangladesh, Myanmar, Nepal	Burkina Faso, Burundi, Central African Republic, Guinea, Haiti, Mozambique, Niger, Sierra Leone, Togo
Rice paddy	Angola, Benin, Burkina Faso, Burundi, Chad, Comoros, Guinea, Guinea Bissau, Madagascar, Malawi, Mali, Niger, United Republic of Tanzania, Togo, Uganda, Zambia	Dem. Rep. of Congo, Mauritania, Mozambique	Central African Republic	Afghanistan, Bhutan, Gambia, Haiti, Liberia, Rwanda, Sierra Leone, Somalia, Sudan
Maize	Benin, Burkina Faso, Burundi, Central African Republic, Chad, Eritrea, Ethiopia, Guinea Bissau, Lesotho, Mali, Mauritania, Mozambique, Sao Tome and Principe, Sudan, United Republic of Tanzania, Togo, Uganda, Bangladesh, Lao People's Democratic Republic, Nepal	Angola, Cape Verde, Dem. Rep. of Congo, Gambia, Madagascar, Malawi, Zambia, Haiti, Yemen	Comoros, Niger, Rwanda, Cambodia	Afghanistan, Bhutan, Guinea, Myanmar, Sierra Leone, Somalia, Vanuatu

Source: UNCTAD LDC Report 1999

VI. Areas Needing Attention

27. In 2000, the Common Fund commenced a survey of all developing country members in order to assess the relative importance and potential of specific commodities. The survey also collated data on the problems experienced in production, processing and marketing to ensure that Common Fund projects were directed to areas of greatest need. Table 4 lists the main non-fuel commodities that were identified by the respondents as being of particular importance to LDCs, either through their contribution to GDP, trade or employment. Traditional commodity production of cocoa, coffee, cotton and sugar continues to be of importance, together with non-traditional sectors such as fish (particularly shell fish).

Table 4. Commodities of Importance to Developing Countries

Commodity	Number of LDCs
Coffee	18
Cotton	17
Fish	13
Livestock/Meat	7
Fruit (all kinds)	6
Cocoa	4
Sugar	4

Table 5. Main Areas of Concern in Production, Processing and Marketing of Commodities

Production	Low productivity technology
	High production cost
	Small scale of production
	Variety degeneration
	Old trees
	Costs of and access to inputs
	Access to, and adoption of, high-yield seeds
	Disease pests
	Climate dependence
	Extension/human capital
Finance	Access to credit
	Low investment (including in R & D)
Processing	Processing technology/capacity
	Low quantity of raw material (supply chain)
Marketing	Falling/volatile prices
	Storage and infrastructure
	Access/trade barriers
	Quality standards (incl. phytosanitary)
	Monopolistic purchasing
	Post-liberalization problems
	Cost of air freight
	Policy/price risk
Other	Power shortages
	Infrastructure
	Environment sustainability

28. Areas of concern in production, processing and marketing are summarized from the survey's results in Table 5. Most observations relate to production and productivity, which is a key component of ensuring continued competitiveness in a climate of declining commodity prices (many respondents cited low world prices as an ongoing problem). Limited access, to inputs and labour-enhancing technologies is reported as one such constraint, either through

the non-availability of improved seeds/inputs or the inability of producers to access credit. The uptake of new production technologies, to deter pests and to boost yields, is a related issue which is of concern to many countries. This can be addressed either at the national level, through improved extension, or at the commodity level with assistance from international organizations such as the Common Fund (a combination of both is likely to have the greatest impact). Quality and sanitary/phytosanitary standards are another recurring theme that affects those engaged in both the production and primary processing stages. Finally, marketing, particularly in a post-liberalization environment, appears to be a problem for some LDCs.

VII. Is Commodity-Dependence Pessimism Justified? The View of the World Bank

29. Having noted the adverse implications on growth and poverty reduction associated with commodity dependence, The World Bank has subsequently identified examples of individual countries which had successfully increased productivity and profitability in specific commodity sectors, often for non-traditional exports, or otherwise significantly increased their processing capacity[8]. The common feature in each of the identified cases related to the ability of the commodity sector to capitalize on the wider reforms undertaken by the respective Government. The most cited of these reforms included eliminating price controls, promoting research and extension, developing transport and communications infrastructure, promoting foreign direct investment and establishing a financial system which can support the commodity sector. However, the implementation of such reforms may be restrained by lack of finance.

30. In cases where returns had been achieved, the Bank found that non-traditional exports had grown significantly and that productivity growth in commodity sectors had improved. This enabled countries to take advantage of the new opportunities for exporting products such as fish, shellfish, flowers and vegetables and to enjoy a price advantage over competitors. The Bank's study therefore shows that it is possible for commodity dependent countries, to diversify horizontally and to gain a renewed advantage in traditional markets through improved productivity. The benefits therefore can be seen to accrue from a "first mover advantage" and may not persist once markets become saturated. This means that those LDCs unable to implement the kind of structural changes necessary will be unable to benefit from opportunities for commodity based growth. The opening up of such opportunities will, however, also depend on the removal of entry barriers (tariff and non-tariff) to the markets of industrialized countries.

VIII. Concluding Remarks

31. LDCs remain highly dependent on commodities for export revenues, employment and an investible surplus. The key to sustained poverty reduction which will permit the attainment of the 2015 development targets is sustained economic growth which is rapid and broad based. One of the most likely sources of pro-poor growth is via commodity development that links agriculture (where the poor are located) and trade (where the opportunities for increased income lie). Commodities provide a strong linkage between the rural poor and the tradeable sector and therefore remain a strategic element in the drive for growth and poverty reduction. The process of globalization, while it is to be welcomed, must therefore be geared to ensuring that the poorest countries are able to take their place in the global marketplace.

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[8] Is Commodity Dependence Pessimism Justified? Yabuki N., Akiyama T, World Bank, 1996.